Lesotho's 2006 budget

The Minister of Finance and Development Planning Timothy Thahane delivered Lesotho's 2006/07 budget speech to parliament on 8 February 2006. It was his third budget statement to parliament.

Changes to the tax incentives

The minister made important changes to Lesotho's tax regime, particularly to stimulate textile and apparel exports. This industry, once the star export performer, is now struggling after the termination of the Agreement on Textiles and Clothing and its restrictions in January 2005. Not only did exports surge between 1999 and 2004, employment rose to a high of over 50 000. Rising employment helped to lower the high poverty levels as unemployment was estimated at about 45% in 2002. The new trade regime has impacted negatively on employment, which fell to 37 500 in 2005, as well as on economic growth, which declined from 3.1% in 2004 to 1.2% in 2005.

The minister proposed that the company tax rate be reduced to 25% from the current 35% as from 1 April. Furthermore, he proposed that the two-tier and preferential company tax rate of 15%, which applies to income from manufacturing and farming, be reduced to zero. The zero rate is also applicable to income from exporting manufactured goods to outside the Southern African Customs Union (SACU). The VAT refund scheme will also be extended. These changes are aimed at supporting the manufacturing sector and attracting new investment.

Revised budget estimates for 2005/06

Revised estimates show that revenue and grants are projected to be higher and expenditures lower than in the 2005/06 budget. A surplus, rather than the budgeted deficit, is therefore expected. SACU revenue, which accounts for about half of total revenue, is expected to be higher than anticipated. On the expenditure side, recurrent as well as capital expenditure is expected to be lower than budgeted. The main reason for the under spending is lower capital expenditure, which is projected to be lower by 28%, rather than recurrent expenditure, which is projected to fall short by 11%. The minister does not hold the view that Lesotho lacks absorptive capacity, but argues that projects funded externally are implemented slowly, whereas projects funded domestically are implemented rapidly. The projected budget surplus is now estimated at 4.2% of GDP in contrast to the budgeted deficit of 2.4%.

Budget allocations for 2006/07

The main proposals are that expenditure should be focused on the development and improvement of infrastructure and utilities, such as roads, water, electricity, communications and health services (clinics and hospitals). Food production will be more commercialised through development of agro-industries. Generally, service delivery in government will be improved. A new parliament will also be built.

Income tax bands will be adjusted by 5% to allow for inflation of 4.6% in the fiscal year. Public servants will receive a 5% salary increase.

Education receives the largest slice at 23.6% of total expenditure (both recurrent and capital). Lesotho offers free primary education. General public services, the next largest, receives 16.5% of the total budget allocation. In terms of recurrent expenditure, education receives 28.5% and general public services 17.2%. In terms of capital expenditure, housing and community amenities receives 28% and other economic affairs 26.4% of this total. A budget surplus of 2.8% of GDP is proposed.

Jan Duvenage ☎(+27 11) 636 4557 ✉ jan.duvenage@standardbank.co.za

Maloti million	2005/2006 Budget	2005/2006 Projected outturn	2006/2007 Proposed budget	2006/2007 % of GDP
Revenue and grants	4,542.8	4,641.1	5,782.2	57.7
Revenue	4,270.2	4,491.2	5,352.4	53.4
Tax revenue	3,709.6	3,984.3	4,794.5	47.8
- of which: Customs	1,983.9	2,306.0	3,087.8	30.8
Non-tax revenue	560.6	506.9	557.9	5.6
Grants	272.6	150.0	429.8	4.3
Expenditure & net lending	4,770.4	4,242.5	5,504.3	54.9
Recurrent expenditure	3,736.2	3,501.9	4,261.3	42.5
- of which: Wages and salaries	1,325.9	1,266.1	1,437.0	14.3
- of which: Interest payments	170.4	123.1	205.7	2.1
Capital expenditure	1,043.4	749.5	1,252.2	12.5
Net lending	-9.1	-8.8	-9.1	-0.1
Overall balance after grants	-227.7	398.6	277.8	2.8

Total expenditure (budget 2006/07)	% of budget
General public services	16.5
Defence	4.5
Public order and safety	9.9
Public health affairs and services	9.3
Social security and welfare affairs	7.6
Education, culture and recreation	25.6
Housing and community amenity	7.8
Economic services	13.2
Other	5.6

The minister pleaded for debt forgiveness to be extended to Lesotho, which is not eligible for the enhanced HIPC initiative. According to IMF data, Lesotho's external debt stock amounted to US$716 million, which is equivalent to 53% of GDP, and the debt-service ratio was 6.8% of exports in 2004/05.

The minister said that public debt of M4.4 billion has been greatly reduced, falling from 100% of GDP in 2000/01 to 54% of GDP today. Interest payments on domestic debt has fallen by 47% from M83.6 million, as budgeted, to M44.5 million as projected in 2005/06. These payments are also projected to be lower by 35% between the 2005/06 and 2006/07 budgets. Interest on foreign debt dropped by 9% from M86.7 million, as budgeted, to M78.6 million as projected in 2005/06. However, foreign interest payments are expected to be 75% higher between the 2006/06 and 2006/07 budgets.

Conclusion

The small landlocked Kingdom of Lesotho faces an extremely serious HIV/Aids pandemic. The minister reiterated that it poses the greatest challenge to the development and indeed the survival of the nation. The nearly 100 000 Aids orphans make up about 5% of the small population of 1.867 million. The budget made provision of M386 million for health services to help combat the pandemic.

The inability of ministries to use funds allocated is an anomaly in a country with such high poverty levels and hence an acute need for social spending.

The lack of capacity to put budget allocations to productive use and the high HIV/Aids infection rate are the major constraints on the country's future economic development. The tax cuts should help improve incentives and raise investment levels, but are unlikely to be sufficient to overcome capacity constraints and the adverse impact of the health crisis.

Group Economics

Goolam Ballim – Group Economist
+27-11-636-2910 goolam.ballim@standardbank.co.za

South Africa

Johan Botha
+27-11-636-2463
johan.botha2@standardbank.co.za

Shireen Darmalingam
+27-11-636-2905
shireen.darmalingam@standardbank.co.za

Rashika Lalla
+27-11-636-6242
rashika.lalla@standardbank.co.za

Elna Moolman
+27-11-631-2018
elna.moolman@standardbank.co.za

Ghana
Nigeria
Tanzania
Cameroon

Robert Bunyi
+27-11-631-1279
robert.bunyi@standardbank.co.za

Botswana
DRC
Lesotho
Namibia
Swaziland

Jan Duvenage
+27-11-636-4557
jan.duvenage@standardbank.co.za

Angola
Egypt
Madagascar
Malawi
Mauritius
Seychelles

Anita Last
+27-11-631-5990
Anita.last@standardbank.co.za

Kenya
Mozambique
Uganda
Zambia
Zimbabwe

Yvonne Mhango
+27-11-631-2190
Yvonne.Mhango@standardbank.co.za

Kindly email brenda.landsberg@standardbank.co.za should you wish to be included on our research distribution list.
Do visit our web site to view our most recent research

Analyst certification
The authors certify that: 1) all recommendations and views detailed in this document reflect his/her personal opinion of the financial instrument or market class discussed; and 2) no part of his/her compensation was, is, nor will be, directly (nor indirectly) related to opinion(s) or recommendation(s) expressed in this document